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IN THE

Supreme Court of the United States

OCTOBER TERM, 1941.

Nos. ~~875-889.~~ 11-19

IN THE MATTER OF

CHICAGO, MILWAUKEE, ST. PAUL AND PACIFIC RAILROAD COMPANY,

Debtor.

GROUP OF INSTITUTIONAL INVESTORS and MUTUAL SAVINGS BANK GROUP,

Petitioners,

vs.

ISRAEL A. ABRAMS, ET AL., Convertible Adjustment Mortgage Bondholders,

Respondents.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Seventh Circuit.

ANSWER OF CONVERTIBLE ADJUSTMENT BONDHOLDERS IN OPPOSITION TO THE PETITION FOR WRIT OF CERTIORARI.

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INDEX.

	PAGE
Answer in Opposition to Petition	1-3
Argument	4-14

SUMMARY OF ARGUMENT.

I. The contention that extensive findings were made by the Commission sufficient to enable the Court to perform its limited function under Section 77 is not supported by the record 4-10

(a) The functions of the Court are not limited and it must form an independent judgment on the fairness of the Plan and whether it complies with the provisions of the Act 4-5

(b) There is no determination and no finding by the Commission as to values on which the courts could perform a limited jurisdiction if it be true that the functions of the courts are limited under the Act 6-10

II. The decision is in accord with the principles announced in the reorganization cases by this Court and does not tend to defeat the purposes of section 77 10-13

III. The decision does not impose requirements that are inconsistent with the statute and with the decisions of this Court 13-14

Cases Cited.

Consolidated Rock Products Co. v. Du Bois, 312 U. S. 510 11

Hamilton Shoe Co. v. Wolf Brothers, 240 U. S. 258 2

Knoxville v. Knoxville Water Co., 212 U. S. 1 7

Morgan v. United States, 298 U. S. 468 14

Tagg Bros. v. United States, 280 U. S. 420 14

United States v. Chicago, Milwaukee & St. Paul, 282 U. S. 311 7

Warren v. Palmer, 310 U. S. 132 5

Western Pacific Railroad Company (C. C. H. S., Par. 53,475) 5

Cases Distinguished.

Louisiana v. U. S., 290 U. S. 70 14

Florida v. U. S., 292 U. S. 1 14

IN THE

Supreme Court of the United States

OCTOBER TERM, 1941.

Nos. 875–883.

IN THE MATTER OF

CHICAGO, MILWAUKEE, ST. PAUL AND PACIFIC RAILROAD COMPANY,

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On Writ of Certiorari to the United States Circuit Court of Appeals for the Seventh Circuit.

ANSWER OF CONVERTIBLE ADJUSTMENT BOND-HOLDERS, RESPONDENTS, IN OPPOSITION TO THE ALLOWANCE OF THE WRIT OF CERTIORARI.

These respondents, holders of Convertible Adjustment Bonds, obtained a reversal of an order approving a reorganization plan of the Milwaukee Road releasing a mort-

gage lien, securing the payment of principal and interest in the amount of $262,423,748, in consideration of no par value common stock to be issued under the plan, without a determination and finding as to the value of the common stock. The order of reversal lacked finality as it remanded the case for a determination and finding as to values (R. 2320).

Primary Issue The primary issue is not as stated in the petition (pp. 7-8), whether it was necessary as "a technical requirement that a formal finding of fact be made", but whether the provision in section 77 (e) requiring a determination of value if "necessary" was mandatory under a plan which did not make the secured creditors "whole" and which proposed to give them securities for a portion of the claim. The issue is whether a plan may be said to be "fair and equitable" when there is no determination and finding as to the value of the new securities to be given in exchange of the old securities. The Seventh Circuit held that under the decisions of this Court, it was mandatory upon the fact-finding body to determine the values and to make appropriate findings.

The Jurisdiction While this Court has jurisdiction to issue the writ, yet in view of the fact that the order lacked finality the application for the writ may be denied on that ground. (*Hamilton Shoe Co.* v. *Wolf Brothers*, 240 U. S. 258; *Simons Co.* v. *Grier Brothers Co.*, 258 U. S. 82, 91.)

Question Presented The real question presented by the record is whether the provisions of section 77 (e) requiring the Commission to determine values if necessary, is mandatory in view of the fact that creditors are asked to release their secured creditors' position and to accept common stock without par value in satisfaction of their debt.

Reasons for the Denial of the Writ. The writ should be denied on the following grounds: (1) the order is not final; (2) the decision is not in conflict with the decisions of this Court or of any other court, and (3) the decision is based on sound equitable principles.

ARGUMENT.

I.

THE CONTENTION THAT EXTENSIVE FINDINGS WERE MADE BY THE COMMISSION SUFFICIENT TO ENABLE THE COURT TO PERFORM ITS LIMITED FUNCTION UNDER SECTION 77 IS NOT SUPPORTED BY THE RECORD.

We challenge the statement (p. 17) that the Court has a "limited function" to "perform" in passing upon the Plan.

(a) The Functions of the Court Are Not Limited and It Must Form an Independent Judgment on the Fairness of the Plan and Whether It Complies with the Provisions of the Act.

The contention of the petitioners (p. 17) that the Court is to perform a "limited function" is contrary to section 77, which provides that the Court shall "hear all parties" and may only approve the Plan "if satisfied" that the Plan is "fair and equitable". This primary duty of the District Court cannot be performed ministerially. It is equally the function of the reviewing court to pass on the findings and the evidence, and the reviewing court's jurisdiction cannot be said to be of a *limited function*. The Opinion correctly stated the rule as follows (R. 2315):

> "It would be begging the question to assume that findings were necessarily made by the I. C. C. when the allocation was made. **We would be delegating to the I. C. C. an obligation which is ours.** The Commission must formulate its plan. It must make fact findings supported by the evidence upon which its plan

> is based. **We must independently determine whether the plan is fair and equitable.** In reaching our conclusion we must ascertain (a) whether there is evidence sufficient to support the findings and (b) we must be able to say that the findings support the plan, and (c) the plan is fair and equitable." (Emphasis ours.)

The Ninth Circuit reached the same conclusion in its decision in Re: *Western Pacific Railroad Company* (C. C. H. S. Par. 53,475) decided November 28, 1941 (not yet officially reported). There, the Ninth Circuit said:

> "In determining whether a plan of reorganization satisfies the requirements of subsection (e), **the court is not concluded by any determination made by the Commission,** but may, and **must, exercise its own independent judgment;** and this is true whether such determination relates to value or to some other subject. Initially, however, the duty of determining the value of any property for any purpose under § 77 rests on the Commission, not on the court." (Emphasis ours.)

Petitioners rely on the decision in the *Palmer* case (308 U. S. 79) in support of their proposition that the Court possesses a "limited function" under section 77. The contrary appears from the opinion of this Court in *Warren* v. *Palmer*, 310 U. S. 132. There, the Court said:

> "The *judicial function of the bankruptcy court* and the *administrative functions* of the Commission work *cooperatively* in reorganization."

It is apparent that the courts may not abdicate their judicial functions in favor of the administrative body and the decision is correct.

(b) There Is No Determination and No Finding By the Commission As to Values on Which the Courts Could Perform, a Limited Jurisdiction If It Be True That the Functions of the Courts Are Limited Under the Act.

Even if it be conceded for academic discussion that the functions of the Court are limited, there is no basis for the statement that the report of the Commission contains "extensive findings" upon which the Court could perform its limited functions.

Value of the Property As a Whole In support of the statement that there are "extensive findings" of the debtor's property as a whole petitioners refer (p. 20) to the Record "R. 2162". The Record states different valuations as to costs of reproduction new, reproduction less depreciation, and the additions and betterments. At another page of the petition the finding of the Commission is quoted (p. 35) as to values including additions and betterments aggregating $662,759,838.00. If the Commission had determined its estimate as to the total value of the debtor's property, there might be some basis for the contention that the Court in the performance of a "limited function" could decide on the evidence whether or not this estimate of the total valuation was supported by such evidence. However, *there is no such determination and no finding.* The Seventh Circuit correctly stated (R. 2315):

> "In the report of the Commission **there is a discussion of the various factors which were deemed pertinent in its inquiry into values.** Absent, however, were clear cut findings or values which are so essential to the intelligent approval of the plan. Our criticism is not directed to the fact that the findings were embodied in the Commission's report (a large part of which is devoted to a discussion and statement of the

evidence) rather than stated specifically as findings. **But the fault lies in the fact that we are left uncertain, or in the dark, as to the finding of the Commission.** The evidence might support a finding of a larger or a smaller amount. **Which should we accept?** The fact finding body is the I. C. C. It must find. We cannot." (Emphasis ours.)

Counsel quote at length (p. 22) from the Report of the Commission dealing with "maximum capitalization". This is not synonymous with valuation. That *valuation and capitalization are distinct* was squarely held by this Court in *Knoxville* v. *Knoxville Water Co.*, 212 U. S. 1, 11. That capitalization and valuation are *distinct*, expressly appears from the opinion of the Interstate Commerce Commission in the former reorganization of the Debtor. In *United States* v. *Chicago, Milwaukee & St. Paul*, 282 U. S. 311, 329, the Court quotes from the Commission's report:

> "In the instant case the testimony is that the value of the properties proposed to be acquired ranges from $640,000,000 to $900,000,000. * * * Against these values or this investment there will be outstanding after the proposed reorganization the following: * * * total $569,116,549. Using the lowest figure, $640,000,000, and deducting from that amount the total par value of the securities enumerated, or approximately $569,110,000, would leave $70,900,000 as representing the value of the 1,174,060 shares of common stock without nominal or par value. * * * Without expressing any opinion as to the value of the no par value common stock, it would appear that upon applying the test suggested there will remain an unmortgaged equity in the properties sufficient to permit the bondholders to assign to the stockholders an interest therein and to support the issue of stock in the amounts proposed."

Even if it be considered that in some instances capitalization denotes valuation, it could not be applied here for the reason that *this capitalization included "no par value*

stock" at a stated value, but not at a real value. The argument of counsel for the petitioners on the exceptions to the examiner's report is well *apropos* here. We quote the following from *their brief* which was filed with the Interstate Commerce Commission (page 11):

> "The Committee's Plan does not propose a total capitalization of $660,000,000. *It is only when the Examiner attaches a value of $100 per share to the no par stock provided by the Committee's Plan that the figure of $660,000,000 is produced. This is an improper treatment in respect to the no par stock under the Plan."*

Value of Convertibles and of of Stock Given in Exchange In support of the contention that the Commission made "extensive findings" as to the value of *each* of the bond issues and of the securities given in exchange thereof, counsel have endeavored to discuss each bond issue under different sub-headings (pp. 29-42). These respondents are only concerned with the Convertible Adjustment Bonds which are discussed in the petition under point "F" (pp. 34-36) and the answer will be confined to such discussion. It is conceded by the petitioners (p. 34) that the Convertibles are "a lien on virtually the entire system" subordinated to other mortgages. They say that the question as to these bonds "was largely whether the total *permissible capitalization*" was such that the satisfaction of the claim of senior creditors "left anything for distribution to these bondholders". The question is not "the permissible capitalization" but *the permissible valuation.* The 50-year Mortgage receives 25% in common stock of no par value in payment of a portion of their debt (R. 2301). If the Commission had determined the value of the 25% of the no par stock and that such securities were only sufficient to compensate the senior creditors for their debt, then there might be some merit in the proposition that the Commission gave to the

Adjustment Mortgage Bondholders whatever was left. However, there is no determination as to the value of the no par common stock. The Commission simply gave this stock a "stated value" of $100 per share, *but no actual value*. How could the Commission have determined what was left for the Convertibles in the absence of a finding as to the value of the common stock which was given to the senior creditors? We have quoted above (p. 8) the argument of the respondents on the proposition that the mere finding that the no par value had a stated value of $100 per share was no determination as to the *real value*. In the face of their own argument, petitioners rely (pp. 34-35) on "the reasoning" of the Commission which fails to distinguish between "stated" value and "real" value. The fallacy of this reasoning is apparent. If the stated value of $100 per share was *actual value*, there may be some logic to the position. The Commission, however, made no finding as to actual value of these shares. *Neither the Commission nor the Court can say what the deficiency will be without a determination as to what the stock was actually worth*. In this connection it might be interesting to examine the statement of the chairman of the proponents of the present plan who said (R. 793):

> "I think the no par common stock which is given in satisfaction of the claims of the adjustment, present adjustment bondholders, has some prospective value. *That value is at the moment highly speculative.*"

He further said (R. 795):

> "As to what value the no par stock has at the reorganization, that depends upon what the actual situation is then."

The cancellation of the secured debt in excess of $262,000,000 by exchange for stock without any definite value and the participation in the common stock by gen-

eral creditors on the arbitrary assumption that the deficiency of the Adjustment Mortgage Bondholders will be $55,000,000 cannot be sustained and the decision correctly reversed the order approving the plan.

The Seventh Circuit properly said (R. 2315):

> "Reluctant as we are to do so, we nevertheless feel that under the decision of this controlling case, there must be a return of the cause to the District Court with direction to the District Court to return it to the I. C. C. and for that body to make the findings on issues vital to the question of values and equities as announced in said Consolidated Rock Products case. **Likewise, the findings must be so specific that the court may definitely see that in the new plan, provision for full compensation of cancelled old senior securities, and all prior preferred positions, is made.** The findings must be sufficiently complete on these matters, that the court may, from its examination, ascertain whether full compensation has been made for the entire bundle of rights which each of the creditors is called upon to surrender." (Emphasis supplied.)

This is in accordance with the settled law as announced by this Court.

II.

THE DECISION IS IN ACCORD WITH THE PRINCIPLES ANNOUNCED IN THE REORGANIZATION CASES BY THIS COURT AND DOES NOT TEND TO DEFEAT THE PURPOSES OF SECTION 77.

The contention (p. 45) that the decision is "in direct conflict" with the decision of this Court in the *Consolidated Rock Products* case (on which the decision rested) is wholly devoid of merit. It is sufficient to say that the Ninth Circuit independently arrived at the conclusion that

the decision of this Court in the *Consolidated Rock Products* case compelled it to reverse a reorganization plan on the precise reasons which were given in the instant case by the Seventh Circuit. *Both courts independently reached the conclusion that a reversal must follow because of the decision of this Court in that case.* In support of their contention that the decision is in conflict with the decision in the *Consolidated Rock Products* case counsel have quoted certain portions from the opinion of this Court. They *omitted*, however, the following (p. 524):

> "We have already noted that *no adequate finding* was made as to the value of the assets of Consolidated. * * *. **A determination of that value must be made** so that criteria will be available to determine a proper allocation of new securities between the bondholders and stockholders in case there is an equity remaining after the bondholders have been made whole."

The opinion of the Seventh Circuit correctly stated (R. 2316):

> "The explicit holding of the *Consolidated Rock Products* case is so mandatory that further discussion is unnecessary. We can not accept the Commission's discussion of the evidence as a finding. Nor may we make findings, save where there is no dispute, or dispute is not serious, in order to sustain the plan."

The same views were expressed by the Ninth Circuit in the *Western Pacific Railroad Company, supra*, where the Court said:

> "To determine the value of the new first mortgage bonds, income bonds, new preferred stock and new common stock mentioned above, it was necessary to determine the value of (1) the debtor's entire property, (2) the property which would be subject to the new first mortgage and (3) the property which would be subject to the income mortgage.

Subsection (e) of § 77 provides: **'If it shall be necessary to determine the value of any property for any purpose under this section, the (Interstate Commerce) Commission shall determine such value and certify the same to the court in its report on the plan.'** In this case, as has been seen, it was necessary to determine the value of (1) the debtor's entire property, (2) each of the claims of Reconstruction Finance Corporation, (3) the claim of Railroad Credit Corporation, (4) the claim of A. C. James Company, (5) the claims of the holders of first mortgage bonds now outstanding, (6) the $10,000,000 of new first mortgage bonds, (7) the $21,219,075 of income bonds, * * * **It thus became the duty of the Commission to determine these values and certify them to the court. That duty was not performed.** (Emphasis ours.)

Lacking the requisite valuation data, the court was in no position to exercise the 'informed, independent judgment' which appraisal of the fairness of a plan of reorganization entails. *Consolidated Rock Products Co.* v. *Du Bois*, *supra*. See, also, *National Surety Co.* v. *Coriell*, 289 U. S. 426, 436; *First National Bank* v. *Flershem*, 290 U. S. 504, 525; *Case* v. *Los Angeles Lumber Products Co.*, 308 U. S. 106, 115. Therefore, instead of approving the plan, the court should have entered an order dismissing the proceeding or, in its discretion and on motion of any party in interest, referring the proceeding back to the Commission for further action."

Counsel refer (p. 48) to the statement of the Court that "an estimate, as distinguished from mathematical certitude, is all that can be made" and that the notion of a "full cash value" for a railroad is "in many respects artificial". The decision in the instant case does not state that it is necessary with mathematical certitude to make findings of values and we do not contend that this is necessary. All that is necessary is to have an estimate. *The Record is barren of such estimate.*

The statement of the petitioners (p. 48) that in the *Consolidated Rock Products* case the principle of the *Boyd* case was violated while here it was not violated because "junior creditors were allowed to participate only to the extent that there was property available, carefully determined by the Commissioner" is not borne out by the record for the reason that we have shown above that there was no determination as to what values the senior creditors received in view of the failure to determine the value of the no par stock.

The Argument (p. 49) that a requirement to determine and find values would defeat § 77 is baseless for the reason that § 77 (e) *expressly provides for a determination of values, if necessary.* It cannot be said *that the compliance with the section operates to defeat it.*

III.

THE DECISION DOES NOT IMPOSE REQUIREMENTS THAT ARE INCONSISTENT WITH THE STATUTE AND WITH THE DECISIONS OF THIS COURT.

The contention (p. 50) that the requirement of the decision for a determination of value and findings is inconsistent with the Statute and with the decisions of this Court are without merit. That it is not inconsistent with the Statute appears from a mere reading of the Act, which specifically provides for a determination of values, if necessary. That it is not inconsistent with the decisions of this Court appears from its numerous decisions that it is necessary to determine values when creditors are not made "whole" and when they are given different securities in exchange of old securities, and in such event determination of values is mandatory. Counsel say (p. 51) that

the reviewing court did not cite "a single case" where this Court indicated "requirement in respect to administrative findings." Section 77 (e) directs the Commission to determine value. We have shown that a determination of value was necessary. The requirement of a determination or finding setting forth the "basic facts" applies to an administrative body under the decisions of this Court (*Morgan v. United States*, 298 U. S. 468, 490; *Tagg Bros. & Moorhead v. United States*, 280 U. S. 420, 442).

Counsel cite (p. 53) the Louisiana case (290 U. S. 70) and quote at length from that decision. The quotation contains the words: "in the absence of some express provision", and Section 77 (e) contains *an express provision for a determination of values*. They also refer (p. 54) to the Florida case (292 U. S. 1) and quote the paragraph which contains the words "the requirement of essential findings as to revenues did not demand an impractical exactness". There is no contention here that in making the findings the Commission was required to make an impractical exactness. The contention is that the Commission had to determine values and to find such values, which it failed to make.

For the foregoing reasons we respectfully submit that the petition for the allowance of the writ of certiorari should be denied.

Respectfully submitted,

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